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December 11, 1997

**Secretary Robert E. Rubin**  
**Department of the Treasury**  
 15th and Pennsylvania Avenue  
 Washington, D.C. 20220

**Re: 31 CFR 208: Management of Federal Agency Disbursement;  
 Notice of Proposed Rulemaking**

Dear Secretary Rubin:

I am writing to comment on the Treasury Department's proposed regulations requiring electronic funds transfer (EFT) of social security, veterans and other benefits or 31 CFR 208. The Woodstock Institute is keenly interested in policies that impact low-income persons. The Institute has a 24-year history of working with community-based organizations, financial institutions, foundations and government to increase access to affordable capital and credit and to promote economic development in low- and moderate-income and minority communities. We have a particular interest in low-income households' access to basic financial services.

There is much to recommend the EFT program. EFT can help low-income people without bank accounts establish relationships with mainstream financial institutions. Using a bank or a credit union brings low-income people into regular contact with financial institutions, encouraging them to use financial services and learn more about financial management. Low-income people will also obtain the same benefits of technology that middle class consumers enjoy: 24-hour ATM and point-of-sale (POS) access to funds. Further, unlike paper checks which may take weeks to replace if lost or stolen, difficulties with EFT can be resolved relatively quickly. EFT also enhances predictability of payments to recipients—allowing immediate access to funds.

However, EFT can effectively serve the interests of low-income people only if several conditions are met. The Woodstock Institute has developed the following recommendations for the proposed EFT regulations. Our intent is to encourage low-income persons to develop mainstream financial accounts, remove barriers to use of financial institutions by the 'unbanked' and encourage banks to extend services to low-income persons.

EFT #193

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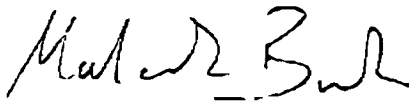
1. **Importance of Mainstream Banking:** Woodstock Institute supports restrictions in the currently proposed regulations that prohibit check cashing outlets from serving as direct recipients of the Treasury Department's transfers. However, we believe that the Treasury Department should also disallow EFT partnerships between regulated institutions and check cashers. Further, we do not support the participation of currency exchanges in the voluntary EFT program. A recent Woodstock Institute study (attached) documents that low-income people who use check cashing outlets pay up to three times as much for basic financial services as bank customers. In addition, there is preliminary interest on the part of the US Post Office to serve as an EFT distribution point. Although this proposal has some merit, we support limiting transfers to depository institutions to encourage non-banked consumers to establish banking relationships.
2. **Consumer Costs:** The Treasury Department has stipulated that ETAs should be provided at a 'reasonable' cost. We are concerned that ETA service fees, as well as the costs of wire transfers, are kept to a minimum. The regulations should establish ceilings on these costs to consumers and should indeed subsidize the cost of transmissions from the Treasury Department to financial institutions out of anticipated EFT savings.
3. **Consumer Protections:** Protections available to other account holders should be available to ETA holders. This includes assurances that account balances can not be attached by creditors and limited liability on the part of account holders in case of theft of ATM or debit cards.
4. **Consumer Education, Outreach and Marketing:** Although the Treasury Department has made provisions to contract with consumer groups and others to help people learn to use ATMs and manage personal finance, many low-income consumers have little or no experience with banks. Some may have attempted to access banks services in the past and been repelled for a variety of reasons. EFT recipients will therefore require significant person-to-person training and education on balancing checkbooks, planning monthly finances, and using an ATM. The Treasury Department should use a portion of the savings of the EFT program, estimated at \$100 million, to fund further educational programs. These programs should be conducted by established consumer and community groups or community development credit unions, experienced with working with low-income persons. Further, financial institutions must commit to providing ongoing, personal assistance.
5. **Access:** Banks and bank regulators should consider the establishment of ETAs by financial institutions an important component of the new Community Reinvestment Act's (CRA) service test. Service innovations, such as establishing mobile bank branches on reservations, rural areas and small towns in under-served areas or in senior citizen buildings should be recognized and encouraged by bank and credit union regulators.

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6. **Waivers:** Individuals with language and literacy barriers as well as mental handicaps should also be eligible for waivers. The EFT options of individuals eligible for federal benefits after to July 26, 1996 and who have bank accounts are unclear. We recommend that the Treasury Department permit them to access an ETA or apply for a waiver if maintaining their current account becomes a hardship.

Thank you for this opportunity to comment on the implementation of EFT. The development of relationships with mainstream financial institutions is critical to low- and moderate-income families improved personal financial management. I believe these EFT recommendations will promote these relationships.

Sincerely,

A handwritten signature in dark ink, appearing to read "Malcolm Bush", written in a cursive style.

Malcolm Bush  
President

MB/ab



# REINVESTMENT ALERT

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Woodstock Institute

March, 1997

Number 10

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## Currency Exchanges Add to Poverty Surcharge for Low-Income Residents

People with low-incomes pay a surcharge for living in less affluent communities because they pay more for goods and services from groceries to insurance. Financial services are no exception. Unfortunately, the costs of financial services are growing just as the share of the U.S. population without a regular bank account is increasing. Studies by the Federal Reserve Board indicate that the number of households with no bank account increased 77 percent between 1977 and 1989, from 6.5 million to 11.5 million.<sup>1</sup> In Chicago, about 20 percent of households have no checking account, forcing many to rely on currency exchanges for basic financial services.<sup>2</sup> A significant proportion of the population uses currency exchanges regularly, and the industry is excessively profitable due to its ability to charge high fees. A recent study found that average rates of return on equity between 1988-91 were 9 percent for national banks, 12 percent for manufacturers, and 104 percent for Illinois currency exchanges.<sup>3</sup> Entry into the currency exchange market is restricted by licensing procedures and it has grown into a noncompetitive industry which secures large profits for existing owners and does little to protect consumers from unreasonable costs.

People who regularly use currency exchanges (CEs) for financial services use them to cash checks, pay bills, or transfer money. CEs can be found throughout the city of Chicago, but are used disproportionately by lower-income and minority individuals. Hispanics are most likely to use CEs, although the highest ratios of CEs to banks are in African-American neighborhoods. This study finds that minorities and lower-income people who use these "fringe banks" pay higher prices for basic financial services. In addition to demonstrating the high costs charged by CEs, this Alert makes recommendations aimed at encouraging greater use of banks by these CE users, at reducing excessive fees charged by CEs, and at increasing consumer awareness of the relative costs of financial services.

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<sup>1</sup> Federal Reserve Board's 1977 *Consumer Credit Survey* and 1989 *Survey of Consumer Finances*.

<sup>2</sup> Metro Chicago Information Center (MCIC), *Community Financial Needs in the Chicago Area*, August, 1996.

<sup>3</sup> John Binder, *An Analysis of CE Check Cashing Rates and the Proposed Decrease in the Maximum Rate for Government Checks*, August 10, 1992. A statement in rebuttal of testimony and evidence presented at the rate hearings on August 19 and 25, 1992.

## Who Uses Currency Exchanges?

The most frequent users of CEs are overwhelmingly minorities and low- to moderate-income individuals.<sup>4</sup> Table I shows community areas which have the highest levels of CE usage and low levels of checking account use. While a mere 2 percent of whites in the Chicago 6-county metropolitan statistical area use CEs for financial services, 28 percent of African-Americans and 32 percent of Hispanics rely on CEs for their regular financial transactions.<sup>5</sup> The percentage of residents of low- and moderate-income neighborhoods who use CEs for financial services is more than nine times greater than the percentage of residents of middle- and high-income neighborhoods who do so.

Table I  
Chicago Communities with the Highest Currency Exchange and Lowest  
Checking Account Use<sup>4</sup>

Communities in PUMA <sup>5</sup>	Percentage Using CE	Percentage Using Checking Account	Median Household Income (1990)	Racial Composition
South Lawndale Lower West Side	58%	24%	\$19,200	75% Hispanic 13% White 10% African-American
Douglas Oakland Grand Boulevard Fuller Park Kenwood Washington Park Hyde Park	47%	44%	\$15,600	77% African-American 14% White 4% Hispanic
Hermosa Avondale Logan Square West Town	37%	43%	\$21,200	54% Hispanic 34% White 10% African-American
Humboldt Park West Garfield Park East Garfield Park North Lawndale	34%	39%	\$20,200	75% African-American 19% Hispanic 4% White
Chicago Metropolitan Statistical Area <sup>6</sup>	10%	81%	\$36,327	71% White 20% African-American 6% Other 3% Asian
City of Chicago	21%	65%	\$26,301	39% African-American 38% White 20% Hispanic

<sup>4</sup> Low-income: under \$21,171; moderate-income: \$21,379-\$34,206; middle-income: \$34,207-\$51,312; high-income: over \$51,312, based on 1990 Census Data.

MCIC, Community Financial Needs in the Chicago Area, August, 1996.

<sup>5</sup> MCIC data, Pooled over a period of 4 years for checking account data and over 5 years for CE data. Data on checking account and CE use refers to percentage of individuals or their spouse/partner who responded to the survey.

A PUMA is a group of community areas adjacent to one another. This designation of communities was chosen because data on checking account and CE usage was available only in this degree of detail. The exact figures for CE and checking account use may vary for each community within a PUMA.

<sup>6</sup> Data on median income and race for the 6-county Chicago MSA from Northwestern Illinois Planning Commission.

These frequent CE users often do not have a checking account to access cash and pay bills. Whereas 93 percent of whites have a checking account, only 57 percent of African-Americans and 47 percent of Hispanic use banks. Similarly, 91 percent of the residents of higher-income areas have checking accounts compared to 56 percent of the residents of low-and moderate-income neighborhoods.

Compared to the metropolitan and city-wide averages, these neighborhoods have a very high percentage of residents who use CEs for financial services. In South Lawndale and the Lower West Side, over half the residents use CEs, compared to 10 percent of all metro Chicago residents. Only one-quarter (24 percent) of residents in these neighborhoods have a checking account compared to 81 percent of metro area residents and 65 percent of city residents. It is interesting to note that Hispanic communities are the most frequent CE users. Even in the moderate-income communities of Hermosa, Avondale, and Logan Square, less than 50 percent of the population has a checking account. We might expect these communities to have a particularly high density of CEs compared to bank branches, but this is actually not the case.

Table II lists the community areas with the highest ratios of CEs to banks or bank branches. The following 12 neighborhoods have the highest ratios of CEs to banks out of Chicago's 77 community areas. City-wide, CEs and bank branches can be found in similar numbers. However, CEs are disproportionately located in lower-income, minority communities. Out of the approximately 400 CEs in Chicago, nearly 100 are located in just 12 communities.

**Table II**  
**Highest Ratios of Currency Exchanges to Banking Institutions by Community<sup>a</sup>**

Community	Numbers of CEs versus Banking Institutions	Median Household Income	Racial Composition
North Lawndale	12:1	\$12,570	96% African-American
Greater Grand Crossing	11:1	\$18,529	99% African-American
West Englewood	10:0	\$22,112	98% African-American
Auburn Gresham	8:1	\$27,547	99% African-American
Englewood	7:1	\$13,243	99% African-American
East Garfield Park	6:0	\$12,082	99% African-American
South Shore	6:1	\$20,094	97% African-American
Roseland	6:1	\$28,601	99% African-American
Grand Boulevard	12:2	\$7,908	99% African-American
Humboldt Park	10:2	\$20,038	49% African-American 44% Hispanic
West Garfield Park	5:0	\$15,102	99% African-American
Hermosa	5:0	\$26,736	69% Hispanic 28% White
City-wide total	404:401	\$26,301	39% African-American 38% White 20% Hispanic

<sup>a</sup> MCIC data, 1994

CEs outnumber banking institutions by as much as 12:1 in North Lawndale and 11:1 in Greater Grand Crossing. In Auburn Gresham, a moderate-income neighborhood, CEs outnumber banks by 8:1. While Hispanics were found to be frequent users of CEs in Table I, Table II shows that the highest CE to bank ratios are in African-American neighborhoods.

### Comparing Currency Exchange and Bank Costs

We surveyed 25 CEs and ten banking institutions to compare fees for financial services. While customers of CEs and banks are charged in different ways for the services they purchase, the fees and services can be compared. CEs charge a separate fee for each transaction, whereas banking institutions may charge a monthly fee for basic services, or a flat fee for certain items, like a box of checks. ATM fees are based on the number and location of transactions and about 25 percent of banks will charge a small fee per check written. All banks surveyed offer a no-minimum balance account. The following table outlines average charges at both CEs and banks for similar services in Chicago lower-income communities.

Table III  
A Comparison of Currency Exchange and Bank Charges

Service	CE charge	Bank charge
Basic monthly fee	\$0	\$0-\$8, depending on average monthly balance
Check cashing	-a \$300 non-public aid check: \$5.10 -a \$300 public aid check: \$4.30 <sup>9</sup>	\$0
Check writing		\$0.20-\$0.30 per check, if charged \$0.07 per check (cost of each check in a box of 200)
ATM		-free within the bank's ATM network -out-of-network ATM fee \$0.50-\$2.00 per transaction -out-of-network ATM may add surcharge for non-customers, \$0.50-\$2.00
Money order	\$0.75 <sup>11</sup>	N/A
Utility bill	\$0.50-\$0.75	

Banking institutions may have several different types of fees for their customers, but the sum of these per month is far less than the total charged at a CE per transaction. The cost of a bank account can range from \$1-\$14 per month, mainly depending on the basic monthly fee. For no-minimum balance accounts, some banks charge a flat \$3-\$4 fee, while other banks charge a slightly higher fee if a customer's average monthly balance falls below \$100-\$250. The amount that a CE charges to cash one check is roughly equivalent to the cost of a checking account per month.

<sup>9</sup> \$300 is estimated to be the average face value of a check received at a CE across the country. According to Illinois regulations, public assistance checks can be charged up to 1.1 percent plus \$0.92, while all non-welfare checks up to \$500 can be charged a maximum of 1.4 percent plus \$0.90. Non-welfare checks over \$500 cost 1.85 percent. In other regulated states, the average fee charged by a check casher is 2 percent to 3 percent of the check's face value. In most states, though, check cashers are unregulated. Some check cashers have been found to charge up to 20 percent of the check's value (Lant, Penny. "Banks make check cashing work" *ABA Banking Journal*, December 1993).

<sup>11</sup> In Illinois, fees for money orders cannot exceed 1 percent of the face value plus \$0.75.

## Comparing Costs for People with Different Incomes and Different Use Patterns

Financial service costs will vary according to income level and frequency of use. We imagined three different low- and moderate-income individuals, and then compared the costs they would pay at a banking institution and at a CE. To quantify what different people pay for financial services, we gathered information on patterns of use of these services to calculate costs of checking accounts and fees at CEs. We assumed that each person receives checks of different value and at different frequencies, will write more checks per month as income rises, and will have an increasing average monthly balance as income goes up. Table IV summarizes the average patterns of use for three people of different income levels.

Table IV  
Typical Use of Financial Services by Income Group

Person	Income	Average frequency of use of financial services <sup>12</sup>
Person A, very low-income	Family of 3, receiving public aid of \$314 per month <sup>13</sup>	Cashes a public aid check once a month, pays 2 utility bills per month, and purchases 2 money orders per month OR writes 4 checks per month.
Person B, low-income	Individual earning \$18,000 per year, and a net monthly income of \$1,170 (\$585 every two weeks)	Cashes a payroll check twice a month, pays 2 utility bills per month, purchases 6 money orders per month OR writes 12 checks per month, uses an ATM 6 times per month, 3 times at their own bank, 3 times at a "foreign" ATM.
Person C, moderate-income	Family earning \$25,000 per year, and a net monthly income of \$1,625 (\$812.50 every two weeks)	Cashes a payroll check twice a month, pays 2 utility bills per month, purchases 8 money orders per month OR writes 19 checks per month, uses an ATM 6 times per month, 3 times at their own bank, 3 times at a "foreign" ATM.

We calculated the costs of CEs and checking accounts at banking institutions in different areas of Chicago. We chose two low-income communities and two moderate-income communities based on racial composition, median income, and ratio of CEs to banking institutions: Grand Boulevard, Logan Square, Auburn Gresham, and North Lawndale. Grand Boulevard, North Lawndale, and Logan Square appear in Table I as communities with high frequencies of CE use and low levels of checking account use. North Lawndale, Grand Boulevard, and Auburn Gresham appear in Table II among the communities with the highest ratios of CEs to banks. Grand Boulevard on the south side and North Lawndale on the west side are low-income, African-American neighborhoods. Auburn Gresham, also predominantly African-American, has the highest median income of \$27,547. Similarly, Logan Square is a moderate-income community; however, it is more ethnically and racially diverse, with a population that is 66 percent Hispanic, 27 percent white, and 5 percent African-American.

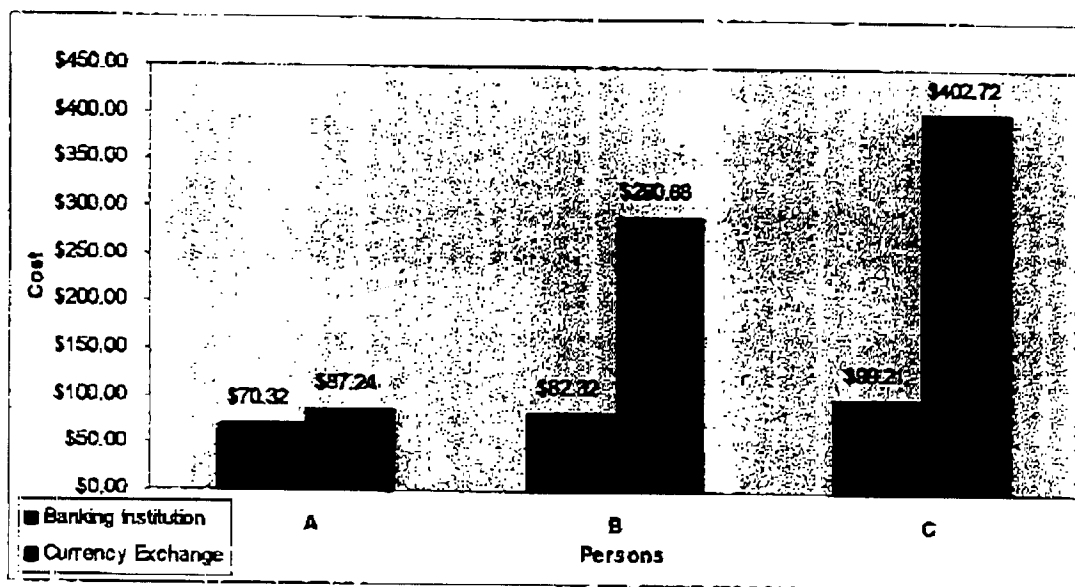
<sup>12</sup> These standards were collected from a variety of sources, including a large Chicago-based bank which provided information on its customer activity and patterns of checking account use for a typical customer with an income of \$18,000 and \$25,000 per year. It is very unlikely that a public aid recipient would have a checking account. It is assumed that this person would write a minimal amount of checks per month to cover basic necessities.

<sup>13</sup> The Illinois Department of Public Aid estimates that the average monthly AFDC grant per family is \$314. They calculated the average AFDC family size to be 2.9.

Each of these neighborhoods has at least one bank or S&L which offers a low-cost checking account with no minimum balance. Neighborhoods with no bank branches were excluded from this analysis. Within these four neighborhoods we located a total of ten bank branches and 50 CEs.<sup>14</sup> Grand Boulevard and North Lawndale have only one banking institution within their boundaries. Auburn Gresham has two banking institutions, while Logan Square, the most racially diverse, despite a lower median income than Auburn Gresham, has six banking institutions.

All banking institutions in these neighborhoods were surveyed for their lowest-cost checking account, and CEs were surveyed for their pricing of check cashing, utility bills, and money orders. We then averaged the costs of using a local banking institution and costs of using a CE among the four communities. These costs are summarized in Table V, which shows annual cost of services and Table VI, which breaks costs down by month and percentage of annual income spent on financial services. Both tables break down costs for the three types of consumers described in Table IV.

Table V  
Average Annual Cost of Financial Services in the Four Communities



As Table V indicates, persons of low- and moderate-income levels are being charged significantly more at a CE than at a banking institution. In consequence, they spend a larger percentage of their income at a CE for the same financial services, as shown in Table VI.

<sup>14</sup> Approximately 80 percent of the data on locations of bank branches, S&Ls, and CE locations was gathered by MCIC. The rest was collected using Chicago phone books by Woodstock Institute. Bank or S&L office locations are examined here. This study does not take into account a banking institution's ATM network or access to banking services by phone.

**Table VI**  
**Average Cost of Financial Services in Four Community Areas per Person**

	Bank/S&L			Currency Exchange			
	Monthly cost	Annual cost	As a percentage of annual income	Monthly cost	Annual cost	As a percentage of annual income	CE cost as a percentage of bank cost
Person A	\$5.86	\$70.32	1.9%	\$7.27	\$87.24	2.3%	24%
Person B	\$6.86	\$82.32	0.5%	\$24.24	\$290.88	1.6%	253%
Person C	\$8.27	\$99.21	0.4%	\$33.56	\$402.72	1.6%	306%

\*The cost at a bank/S&L does not include an opening deposit (average \$148), a one-time deposit that may be withdrawn immediately.

For very low-income people, these financial service costs take a significant share of income. Person A spends about 40 percent more than the portion of income spent by Person B or C on financial services at a CE. CE costs for Person A are even greater than checking account costs for person B. Persons B and C, whose bank expenses would cost between \$80-\$100 per year, would spend nearly four times as much on services at a CE.

## Conclusions

A bank customer benefits from more than these basic financial savings on check cashing and writing. Using a bank brings customers into regular contact with conventional financial services providers. This regular contact is a benefit in itself through which people learn about other bank services and develop familiarity with these institutions. Consumers who access financial services at banks, S&Ls, or credit unions benefit by saving money, earning interest, and keeping funds secure, as well as by reducing the cost of check writing and cashing. This entree to financial services can help to establish a credit history and provide access to personal loans or home mortgages. The combination of lower costs and significant service advantages are powerful reasons for promoting greater use of bank services. Another powerful reason for the expansion of bank services to lower-income communities is the federal law mandating the electronic transfer of funds for recipients of federal money, including public aid.

As this study has shown, lower-income residents of Chicago tend to use CEs over bank checking accounts. Since bank location alone cannot account for low usage of checking accounts in lower-income neighborhoods, our recommendations address the various conditions which contribute to CE use over checking account use. These recommendations encourage greater use of banks instead of CEs, and address the regulation of banks, regulation of CEs, and consumer education.

1. More effective implementation of federal and state bank regulations to encourage increased presence in lower-income and minority communities and to offer low-cost financial services

**Woodstock Institute**

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Federal Law

- Aggressively apply the service test in evaluating banks under the recently revised CRA regulations.
- Encourage banks to offer basic low-cost checking accounts without unreasonable deposit requirements
- Encourage banks to locate branches and ATMs in lower-income and minority communities
- Encourage banks to increase outreach to lower-income and minority communities

Encourage banks to distribute public aid electronically to increase access to banking services to very low-income people

State Law

- Develop linked deposit program in which the deposit of state funds would reward banks for serving low-income and minority communities, including creative outreach and marketing<sup>15</sup>
  - Develop state regulations requiring that state-chartered banks offer reasonable, low-cost services to customers in service area<sup>16</sup>
2. More effective regulation of CEs by the Illinois Department of Financial Institutions (DFI)
- Lower the maximum rates CEs may charge to cash checks and sell money orders
  - Allow freer entry into CE market to permit greater competition
3. Consumer education to increase awareness about the real costs of financial services

Financial institutions, currency exchanges, consumer or neighborhood groups should:

- Educate consumers about the costs of CEs and banks through a state regulation which would require CEs to distribute literature informing people of the comparative costs of financial services

<sup>15</sup> See *More for Our Money: A Primer on Public Deposit Programs*, by Valjean McLoughlin and Malcolm Bush, Woodstock Institute, 1994.

<sup>16</sup> Both New York and New Jersey have laws which require state-chartered banks to provide "lifestyle" or low-cost checking accounts with no minimum balance (a \$50 minimum balance must be maintained in NJ), no more than a \$3 monthly fee and at least 8 free transactions per month if they already offer regular checking accounts ("Banking Banking: The 1995-96 Consumer Bank Scorecard", Public Advocate for City of New York, January 1996).

**Woodstock Institute**

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- Provide seminars on basic financial services, including budgeting, saving, and balancing a checkbook
- Identify other potential benefits of using a bank, such as earning interest on savings and building a credit history

These steps will reduce an important component of the poverty surcharge for residents of lower-income neighborhoods.

Prepared by  
Erin Mullen,  
Malcolm Bush, and  
Samantha Weinstein